No. 959

IN THE

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, [illegible]

[illegible] VAN BERGEN, [illegible]

vs.

[illegible] INSURANCE CORPORATION OF AMERICA, [illegible] GOODE, CLYDE H. BELLAMY, [illegible] LEWIS, JR., [illegible] ADRIAN S. WRIGHT, [illegible] W. MEEKS WRIGHT, [illegible] HENRY D. [illegible], [illegible] LAWRENCE H. BIRD, [illegible] HERBERT H. ZIMMERMAN, and [illegible] ROBERT THOMAS, [illegible],

BRIEF FOR RESPONDENTS IN OPPOSITION

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No. 959

IN THE

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1958

L. BRYAN BERGESON, *Petitioner,*

vs.

LIFE INSURANCE CORPORATION OF AMERICA, a corporation; CLEO H. BULLARD; LEWIS R. RICH; ADRIAN S. WRIGHT; W. MEEKS WIRTHLIN; HARRY D. PUGSLEY; LAWRENCE H. BIRRELL; HERBERT J. ZIMMERMAN; and J. ROBERT THOMAS, *Respondents.*

BRIEF FOR RESPONDENTS IN OPPOSITION

INTRODUCTORY STATEMENT

Reference to the opinions below and the jurisdictional requisites are adequately set forth in the petition. Petitioner grasps for issues for Supreme Court determination and for statutes and regulations involved. Those set forth in the petition are illusory as a brief examination of this case will demonstrate.

STATEMENT

Petitioner, the purchaser of 83 shares of stock in respondent Life Insurance Corporation of America, brought a de-

rivative stockholder's suit against respondents Bullard, Rich, Wright, Wirthlin and Pugsley, former directors and against respondents Birrell, Zimmerman and Thomas, former accountants of the corporation.

The facts are not in dispute, but we believe a restatement is necessary for the understanding of the Court.

In 1951 two organizations were formed under Utah law, one a partnership, designated as Licoa Agency and herein referred to as the "partnership," the other a corporation, being respondent Life Insurance Corporation of America, and herein referred to as the "corporation." The corporation was organized as a mutual insurer. The members of the partnership and the directors of the corporation were substantially the same. The partnership had two principal functions (a) to provide funds for the corporation to enable it to carry on its affairs, and (b) to act as a general agent for the corporation in selling insurance.

The corporation thereafter amended its articles of incorporation to authorize it to act as a stock insurer and sought a certificate from the Utah Insurance Commissioner authorizing it to so act. In order to obtain such certificate it was necessary for the corporation to meet certain capital requirements imposed by Utah law. The corporation employed the accountants to perform certain services in connection with procuring such certificate.

The corporation represented to the Insurance Commissioner that it had met the capital requirements, and the desired certificate was issued. Thereafter, the Insurance Commissioner determined that the corporation's capital was impaired. This impairment led to a reorganization of the

corporation whereby new stock was issued on a basis of one share for each 13.5324 shares of old stock outstanding, and $200,000.00 of new capital was supplied by Bankers Life and Casualty Company which presently owns approximately 90% of the stock of the corporation.

No creditor or policy holder is in any way involved in this litigation nor is any complaint being made respecting the reorganization of the corporation.

In 1954 a settlement was made between the partnership and the corporation whereby the partnership surrendered its claims for money advanced and equipment furnished to the corporation and for commissions accrued under its agency contract and took stock in the corporation on a basis of $20.00 per share, which was thereafter transferred to members of the partnership on liquidation.

Prior to commencement of this suit the respondent directors had been replaced by others and respondent Pugsley brought suit in state court against the corporation for director's fees. The state court acquired jurisdiction over the corporation which was there represented by counsel. That litigation was settled between Pugsley and the corporation, pursuant to stipulation and judgment entered dismissing the action with prejudice together with any possible counterclaims relating thereto.

Petitioner brought this suit in two counts. On the first count petitioner claimed damages against the directors and accountants for negligently causing the corporation to be qualified as a stock insurer without the requisite capital and on the second sought recovery against the directors for the value of the stock issued in the partnership settlement.

Pugsley undertook to plead the judgment of the state court as a bar, and petitioner moved the District Court to enjoin him from doing so.

Upon consideration of the issues the District Court held that: (a) Petitioner failed to state a claim on the first count; (b) Pugsley was entitled to plead the judgment of the state court as a bar; and (c) neither the money advanced and equipment furnished to the corporation by the partnership nor the commissions accrued on insurance written by the partnership was lawful consideration for the issuance of the stock to the partnership and that the directors, other than Pugsley, were liable for the value of the stock as prayed.

On appeal the Court of Appeals for the Tenth Circuit affirmed the judgment of the District Court on the first count and on the Pugsley defense, but held on the second count that in connection with the issuance of the stock credit should be allowed the directors for money advanced and equipment furnished to the corporation, but not for commissions accrued and directed that judgment should be modified accordingly.

ARGUMENT

I

NO GROUND EXISTS FOR DISTURBING THE DECISION BELOW.

(a) The Decisions on Petitioner's First Count are Clearly Correct.

Petitioner brought his first count on a nebulous theory that the corporation was damaged because its directors and accountants negligently caused the corporation to obtain a

certificate to act as a stock insurer without sufficient capital. As indicated above, the corporation was organized as a mutual insurer. It sought to obtain a certificate from the Insurance Commissioner of the State of Utah to enable it to act as a stock insurer. In order to obtain such certificate it was required under Utah law to have capital of $125,000.00. The corporation obtained its certificate although its capital may have been inadequate to meet the statutory requirement. No Utah case or statute has been cited by petitioner in support of his theory that the corporation has a claim under such circumstances. Petitioner undertook to invoke the doctrine in *Old Dominion Copper Mining and Smelting Co.* v. *Bigelow*, 203 Mass. 159, 89 N. E. 193, and *Hayward* v. *Leeson*, 176 Mass. 323, 57 N. E. 656. The rule announced in these cases is at variance with the decision of this Court in *Old Dominion Copper Mining and Smelting Co.* v. *Lewisohn*, 210 U. S. 206 (1908). This difference is, however, entirely immaterial here. The foregoing cases involved situations where promoters obtained secret profits in transactions with corporations. No secret profits are involved in the case at bar. The corporation sought a certificate to act as a stock insurer. It secured what it sought. No case has been found which confers a right upon a corporation to sue under such circumstances and we think none can be found, for upon principle the decisions of the District Court and the Court of Appeals are clearly correct.

(b) The Decisions Below With Respect to the Pugsley Defense Are Likewise Clearly Correct.

Petitioner seeks to avoid the provisions of the Act of June 25, 1948, 62 Stat. 968, 28 U. S. C. A. 2283, and to prevent Pugsley from invoking the judgment of the state

court under the decision of *Wells Fargo and Company* v. *Taylor*, 254 U. S. 175 (1920). The rule of that case rests upon the equitable doctrine that a party may be prevented by a court of the United States from enforcing a state court judgment where such enforcement would be contrary to recognized principles of equity and the standards of good conscience.

There Taylor, an express company employee who assumed all risk of injury incident to his employment, recovered a judgment against a railroad company in state court in a suit in which the express company was prevented from being heard. The express company was obligated to indemnify the railroad company against Taylor's claim and Taylor was financially irresponsible. In a suit, by the express company against Taylor in a court of the United States, it was held that Taylor could not in equity and good conscience enforce his state court judgment and was enjoined from doing so.

None of the controlling facts in *Wells Fargo and Company* are present here. The state court acquired jurisdiction of the corporation. It was there adequately represented by counsel. No fraud or collusion is suggested. There is no contention that the other parties defendant are not financially responsible or that any judgment recovered here cannot be satisfied by such defendants. In short, there is nothing here to indicate that the dropping of Pugsley as a party defendant in any manner prejudiced the petitioner, or any reason why in equity and good conscience the judgment of the state court should not be pleaded as a bar.

The Memorandum Decision of District Court Judge, A. Sherman Christenson, at page 20 thereof, states:

> "Harry D. Pugsley was also joined as a defendant. He was a member of the partnership and director of the corporation during the times in question. Prior to the beginning of this suit, Pugsley brought an action in the Third Judicial District Court of the State of Utah in and for Salt Lake County against the corporation for unpaid fees. The corporation, either orally, or by written pleading (it is not clear which) claimed negligence on Pugsley's part. The case was then compromised and settled and an order entered dismissing with prejudice all claims of the parties. This heretofore has been determined by me to be a valid judgment and summary judgment has been granted on the ground that that case was res judicata here in Pugsley's favor."

The decision of the Tenth Circuit Court of Appeals, pages 30-31, thereon states:

> "Defendant Pugsley asserts the defense of res judicata and obtained a summary judgment in his favor. The basis of his defense is a judgment of dismissal entered on stipulation of counsel by a Utah court on March 7, 1957, dismissing an action brought by Pugsley against the company to recover unpaid director's fees. The judgment states that the action, 'together with any possible counterclaims relating thereto,' was dismissed with prejudice. The claim here asserted against Pugsley was one which could have been raised by the company as a counterclaim in the state court suit. This is not questioned by the plaintiff. Instead he urges that the company had no right to make the stipulation upon which the judgment was entered without the approval of the stockholders and such approval was never obtained. The point is of no avail as the state court unquestionably had jurisdiction of the parties and of the subject mat-

ter and had power to enter the judgment which it did. A judgment of dismissal pursuant to a stipulated settlement is ordinarily a judgment on the merits barring another action for the same cause. No suggestion is made of fraud or collusion. Whatever claim there may be of lack of corporate power in the absence of stockholder action should be addressed to the Utah court. At the most it is a collateral attack on the judgment which may not be made here."

(c) No Ground Exists for Disturbing the Decision on the Second Count.

Respondents Bullard, Rich, Wright and Wirthlin appealed from the judgment of the District Court on the second count. These respondents in good faith believed and urged upon the Court of Appeals the proposition that the entire issuance of stock to the partnership was supported by a valid consideration. The Court of Appeals concluded that as to the advances of moneys and the furnishing of equipment which had been made by the partnership to the corporation, good consideration existed for the issuance of stock, but because of provisions of Utah law deemed controlling, reached a contrary conclusion with respect to commissions which the partnership claimed for insurance written in the corporation.

The holding of the Court of Appeals that money advanced and equipment furnished to the corporation by the partnership was good consideration for the issuance of stock is entirely correct upon principle and for reasons which fully appear from that portion of its decision hereinafter set forth.

II

THERE IS NO CONFLICT OF DECISIONS.

(a) There is no Conflict with *Wells Fargo and Company* v. *Taylor.*

Petitioner asserts that the decision of the Court of Appeals is in conflict with *Wells Fargo and Company* v. *Taylor, supra.* As we have shown the decision in that case prevents a party from enforcing a state court judgment where its enforcement would be contrary to equity and good conscience. Petitioner has shown no ground here for invoking equity. There is no conflict with *Wells Fargo and Company.*

(b) There is no Conflict with the Decisions of Other Courts of Appeal.

Petitioner asserts a conflict of decision because of the determination of the Court of Appeals that for the purposes of its decision there was a single entity in the corporation.

The Court of Appeals held in part as follows:

> "Plaintiff contends that at the time of the conversion from a mutual insurer to a stock insurer a new corporate entity came into being. While there are important differences between a mutual insurer and a stock insurer, (citing cases) Utah recognizes the right of a mutual company to change to a stock company. (Citing Utah Statutes.) The uncontradicted statement of defendant Bullard in his deposition was that the plan of the promoters of the company was to organize a 'mutual company, to use that as the basis of the corporation, and then to convert it at a later date to the stock company.' Such plan was recognized in the original by-laws which set up pro-

cedures to be followed in the event 'the corporate structure is changed to a capital stock insurer.' The necessary amendment to effect the change was unanimously adopted by the members. There was no change of either name or officers. The mere amendment of articles of incorporation does not create a new corporation (citing cases and texts). This rule has been applied to the reorganization of insurance companies. (Citing cases and texts.)

"The partnership admittedly advanced cash and furnished equipment to the company in the total value of about $28,000. The trial court held that this did not constitute consideration for the stock issue because of the inhibitions contained in the Utah statutes with reference to the borrowing of money by a mutual insurer. Among other things, the Utah law forbids the payment of a loan by a mutual except out of earned surplus. (Citing Utah Statute.) The trial court held in effect that the sums represented by the cash advanced and equipment furnished were loans to the mutual repayable only out of earned surplus, and that as there was no earned surplus at the time of the conversion to a stock insurer the advances were uncollectible from the mutual and did not automatically become a liability of the stock insurer.

"Defendant Bullard testified that the original contributions by the partnership found their way into the books of the mutual as contributed surplus 'on the understanding that at such time that the mutual corporation became a stock corporation that that would then be issued back to the LICOA Agency for stock.' This can only mean that the advances were not loans but were in effect stock subscriptions. As there was only one entity, the acceptance of the benefit of these advances carried with it the obligation to issue stock therefor at such time as the corporation was in a position to take such action. To the extent that stock was issued with a market value not exceeding the value of the cash advanced and the

equipment furnished it was paid for by the partnership."

Petitioner asserts that the foregoing holding is in conflict with *Equitable Life Assurance Society* v. *Bowers*, 87 F. 2d 687 (C. C. A. 2, 1937), *Driscoll* v. *Washington County Fire Insurance Co.*, 110 F. 2d 485 (C. C. A. 3, 1940), *Ohio Farmers Indemnity Co.* v. *Commissioner of Internal Revenue*, 108 F. 2d 665 (C. C. A. 6, 1940), and *Hutchins Mutual Insurance Co. of District of Columbia* v. *Hazen, et al.*, 105 F. 2d 53 (D. C. Ct. of App., 1939).

Such asserted conflict is wholly without merit. The Court of Appeals pointed out that there are important differences between a mutual insurer and a stock insurer and cited both *Ohio Farmers Indemnity Co.* v. *Commissioner of Internal Revenue* and *Hutchins* v. *Hazen*, *supra*, to so demonstrate. Such differences are further demonstrated by *Equitable Life Assurance Society* v. *Bowers*, *supra*, which involved a consideration of the question of whether Equitable should be taxed as a stock company or a mutual company under a revenue act.

As shown from the foregoing cases the differences which exist between a mutual insurer and a stock insurer have been recognized in the application of revenue acts and in the administration of regulatory statutes. These differences, however, have no application in the instant case where the issue was simply whether money advanced and equipment furnished to a mutual insurer was good consideration for stock issued by the corporation after it had converted to a stock insurer. No conflict of decision in the determination of that question has been shown.

(c) There is no Conflict with the Decisions of this Court in the Application of the Federal Rules of Civil Procedure.

Petitioner asserts a conflict with the decisions of this Court in the application of Federal Rules of Civil Procedure, Rule 52(a), 28 U. S. C. A.

This is a secondary action brought by a shareholder under Federal Rules of Civil Procedure, Rule 23(b), 28 U. S. C. A., which was adopted from the preceding Equity Rules 94 and 27. Equity Rule 94 was adopted as a result of *Hawes* v. *City of Oakland*, 104 U. S. 450 (1882). Suits brought under this rule are equitable in nature. 3, Moore's Federal Practice, Paragraphs 23.15-23.23 (2d Ed. 1951). In equity cases findings of fact have been reviewable both as to the weight of the supporting evidence and the sufficiency. Review has been both of law and fact. Rule 52(a) is based on and substantially carries forward the former equity practice. 5, Moore's Federal Practice, Pargraphs 52.01-52.02 (2d Ed. 1951). *United States* v. *United States Gypsum Co.*, 333 U. S. 364 (1948).

Petitioner asserts that the Court of Appeals based its decision upon a set of facts in complete conflict with the facts before the trial court. Petitioner fails to point out wherein lies this complete conflict of facts. Actually, as the Court of Appeals observed, there is not a single disputed fact issue in this litigation; but if there were a fact issue involved the Court of Appeals was empowered under Rule 52(a) to resolve it. The District Court and the Court of Appeals in considering the second count of petitioner's complaint, with no fact in dispute, were called upon to determine whether

the money advanced and the equipment furnished by the partnership to the corporation constituted valid consideration for the issuance of stock. The District Court concluded that it did not. The Court of Appeals, for the reasons hereinabove set forth concluded that the corporation in converting from a mutual insurer to a stock insurer continued as an entity and reached a contrary result. It is this determination which petitioner assails. Such determination was in no sense a finding of fact. It was simply a conclusion of law reached upon a consideration of undisputed facts. It is elementary that an appellate court is not by Rule 52(a) in any degree concluded by a trial court's view of the law. 5, Moore's Federal Practice, Paragraph 52.03(2) (2d Ed. 1951); *United States* v. *United States Gypsum Company*, 333 U. S. 364, 396.

The decision of the trial court on the first count was by summary judgment and therefore Rule 52(a) would have no application. No procedure taken here conflicts with the principles of *United States* v. *Yellow Cab Co.*, 338 U. S. 338 (1949), or *United States* v. *Oregon State Medical Society, et al.*, 343 U. S. 326 (1952) and there is no substance whatever to the contentions of petitioner that the Court of Appeals violated the provisions of Rule 52(a).

III

THERE IS NO CONFLICT WITH APPLICABLE STATE LAW.

It is asserted by petitioner that there is a conflict between the decision of the Court of Appeals and applicable state law. While petitioner cites certain sections of the Utah

statutes dealing with insurance companies, no case is cited indicating any conflict, and none is shown to exist.

It is asserted that the Court of Appeals failed to apply the rule of *Old Dominion Copper Mining and Smelting Co.* v. *Bigelow*, *supra*. We cannot understand how the Court of Appeals was obligated to apply the doctrine of that case in the absence of its approval by a Utah court. Moreover, as the Court of Appeals pointed out the doctrine of the *Bigelow* case is inapplicable to the facts involved here.

It is asserted that the Court of Appeals failed to apply Utah law with respect to the duties of fiduciaries, but no Utah case has been cited in support of such assertion, and the citations to general corporation law are of no importance.

CONCLUSION

This case involves local issues under local law. It is not a case of general importance. It was carefully considered by the trial court and the Court of Appeals. Their decisions differ on only one phase of the second count: While respondents Bullard, Rich, Wright and Wirthlin on appeal urged a different result on the second count, they cannot now complain. The decisions of which petitioner complains were correctly made. Though petitioner grasps for issues to present for the review of this Court those asserted are without substance or merit. The petition should accordingly be denied.

Respectfully submitted,

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